



Montana Legislative Services Division
Legal Services Office

SENATE FINANCE & CLAIMS

Exhibit No. 3
Date 3-30-15
Bill No. HB 2
PO BOX 201706
Helena, MT 59620-1706
(406) 444-3064
FAX (406) 444-3036

TO: President Barrett
FROM: Julie Johnson, Staff Attorney
RE: DNRC Lease
DATE: January 14, 2015

You have asked a number of questions related to the construction of a building to be leased to the Department of Natural Resources and Conservation (DNRC).

BACKGROUND

The property where the building will be constructed is located on 11th Avenue, just north of the Capital Hill Mall. The previous structure on the property was recently demolished and had been unoccupied since 2010 due to health concerns. The State Board of Land Commissioners approved the acquisition of the property from Department of Administration in December of 2012. According to DNRC, an appraisal of the property at that time determined that the land was worth more without the building and noted that: "Maximum productivity of the subject site would be for redevelopment with a new office or retail building that is commensurate with the current land values in the neighborhood." According to the department, the Land Board paid the Department of Administration the appraised value of the land less the anticipated demolition costs.

Lease of Land

The DNRC also reports that the standard procurement and commercial lease processes were followed. A Request for Proposal was issued in the spring of 2014 and awarded to Dick Anderson Construction in the fall of 2014. The accepted bid proposed to demolish the building and construct a three-story building with a two-story parking structure. According to the DNRC, the lease on the property is expected to generate \$45,000 in annual revenue for Montana University System and will increase during the term of the lease.

Building Lease

The new construction will house the Department of Natural Resources and Conservation. The lease between Dick Anderson Construction and the DNRC is for 20 years and is for 39,085 square feet at an annual cost of \$24.75 per square foot. The total annual lease cost in the new building will be \$967,354. This compares to a current total annual cost of \$796,815, or \$18.78 per square foot. This figure includes an anticipated lease of 12,175 square foot in addition to its present location at 1625 Eleventh Avenue.

LETTERS OF REFERENCE & CLAIMS

1. Name of the person referred to

2. Address of the person referred to

3. Date of the reference

LAW

Article X, sec. 4, of the Montana Constitution provides that the Board of land commissioners "has the authority to direct, control, lease, exchange, and sell school lands and lands which have been or may be granted for the support and benefit of the various state educational institutions, under such regulations and restrictions as may be provided by law."

Article X, sec. 10, of the Montana Constitution provides that "rent from leased lands or properties, shall be devoted to the maintenance and perpetuation of the respective institutions [of the Montana university system]."

Montana law allows a state agency to enter into a lease agreement without legislative approval as long as: 1) the lease is for no more than 40,000 square feet; and 2) the term of the lease is 20 years or less. 2-17-101(5), MCA. Leases involving more than 40,000 square feet or having a term exceeding 20 years must be submitted as part of the long-range building program and approved by the legislature before the lease may proceed. 2-17-101(5), MCA.

Montana law requires legislative approval for the construction of a building in excess of \$150,000. However, this provision does not apply to a private entity building on land leased from the state.

CONCLUSION

The Land Board is authorized to lease the property under the Constitution. The DNRC is authorized to enter into a lease for the new building under 2-17-101(5), MCA, because the term of the lease does not exceed 20 years and the square footage to be leased is under the 40,000 square foot limit. Explicit legislative approval for a lease under these terms is not required.

Funding for the lease would come from the same source as its payments for DNRC's current location, out of its operations budgets.

Please let me know if you have any further questions or would like further research on a particular issue.

DNRC Rent Comparison - Existing Building with Additional Space, New Building

Existing Office Space:

Current Square feet		Year	Office	Storage	
Office	29,325 sq.ft	2014	\$14.25	\$7.13	\$4.04
Storage	600 sq.ft	2015	\$14.25	\$7.13	\$4.20
Utilities	\$120,941 per year	2016	\$14.25	\$7.13	\$4.37

2016 per square foot charge: \$18.48 per sq. ft
 2016 Square foot: 42,100 sq.ft
 Annual Rate Increase: 4%

Existing building all floors: 42,100 sq. ft.

YEAR	% INCR	RATE	Annual Payment
1	4%	19.22	\$ 809,062.53
2	4%	19.99	\$ 841,425.03
3	4%	20.79	\$ 875,082.03
4	4%	21.62	\$ 910,085.32
5	4%	22.48	\$ 946,488.73
6	4%	23.38	\$ 984,348.28
7	4%	24.32	\$ 1,023,722.21
8	4%	25.29	\$ 1,064,671.10
9	4%	26.30	\$ 1,107,257.94
10	4%	27.35	\$ 1,151,548.26
11	4%	28.45	\$ 1,197,610.19
12	4%	29.58	\$ 1,245,514.60
13	4%	30.77	\$ 1,295,335.18
14	4%	32.00	\$ 1,347,148.59
15	4%	33.28	\$ 1,401,034.53
16	4%	34.61	\$ 1,457,075.91
17	4%	35.99	\$ 1,515,358.95
18	4%	37.43	\$ 1,575,973.31
19	4%	38.93	\$ 1,639,012.24
20	4%	40.49	\$ 1,704,572.73
			\$ 24,092,327.64

New building, 39,085 sq. ft.

Year	Rate	Annual Payment
1	24.75 \$	967,353.00
2	24.75 \$	967,353.00
3	24.75 \$	967,353.00
4	24.75 \$	967,353.00
5	24.75 \$	967,353.00
6	26.48 \$	1,034,970.00
7	26.48 \$	1,034,970.00
8	26.48 \$	1,034,970.00
9	26.48 \$	1,034,970.00
10	26.48 \$	1,034,970.00
11	28.21 \$	1,102,587.00
12	28.21 \$	1,102,587.00
13	28.21 \$	1,102,587.00
14	28.21 \$	1,102,587.00
15	28.21 \$	1,102,587.00
16	29.94 \$	1,170,204.00
17	29.94 \$	1,170,204.00
18	29.94 \$	1,170,204.00
19	29.94 \$	1,170,204.00
20	29.94 \$	1,170,204.00
		\$ 21,375,570.00

Savings over 20 year lease period =	\$2,716,758
Taxes to L&C county @ \$90,000 per year =	\$1,800,000
Payment to the Trust, benefit UofM, MSU =	\$1,022,828
Total Savings	\$5,539,586



Contact: John E. Tubbs Director
 jtubbs@mt.gov, 406-444-2074

3/4/2015

[illegible]

Speaking Points

1)Parking Garage--It was stated that DNRC was out of compliance with MCA 2-17-101 ---the requirement to get legislative approval on leased building over 40,000 sq. ft. They stated that the garage was included in this computation making it exceed the 40,000 sq. ft. maximum. This statement is not accurate. Lessor was required to provide adequate parking, a parking garage was the contractors proposal to provide adequate parking.

In the lease section 2 it states:

"2. PREMISE DESCRIPTION

The space being leased (leased premise) is approximately 39,085 square feet, and includes the right to use common areas within the leased premise. The leased premise will be constructed and located at Lot D, Cannon CW Addition to the City of Helena, 1539 11th Avenue, Helena, Montana."

This section does not mention the garage. DOA did not request a parking garage. Dick Anderson was only required to provide "adequate parking" as stated in Section 7 :

"7. PARKING SPACE

Lessor shall provide adequate parking spaces, including the requisite number of handicapped spaces in compliance with the Americans With Disabilities Act, as part of the leased premise at no additional charge or cost to the Lessee."

DA chose to have his parking requirement be a parking garage but DOA did not request a parking garage.

2)Capitol Complex Advisory Council---the committee stated DNRC was out of compliance with the "Capitol Complex Board." There is no "Board" that could be found so assume they were speaking about the Capitol Complex Advisory Council. This council is advisory only and once DNRC purchased the land/building form DOA it was transferred to DNRC's Trust Division and thus would no longer be under the Capitol Master Plan or Council Advisory.

3)\$150,000 building cost needing legislature consent---It was stated that DOA/DNRC violated MCA statute because legislative consent was not received for

buildings costing more than \$150,000. 18-2-101, (b) (iii) states "Building" does not include a building, facility or structure leased or to be leased by a state agency.

4) Rental Rate:

According to statute 77-1-905, the minimum rental rate needs to be at a percentage of the appraised value which is equal to at least 2% less than the Board of Investment's unified investment program's return. In this case the Board of Investment's return was 6%; which lead to a statutory minimum bid of 4% of the appraised value. The Department chose to set the minimum bid for the RFP higher than what was statutorily required due to market conditions in the Helena area. The Department set the minimum bid at 5% of the appraised value.

The actual rental rate that was proposed in the response to the RFP is calculated at 6.7%. This is the highest rate we have ever received for a large commercial ground lease.



Montana Department of Natural Resources & Conservation
Trust Land Management Division
Real Estate Management Bureau

February 26, 2015

Former Corrections Office Site Redevelopment Project- Timeline.

- September 2005- Department of Corrections forced to vacate the basement of what once was the Intermountain Union College Dormitory (aka Mills Hall), as it was condemned.
- August 2010- Department of Corrections vacates Mills Hall and relocates to old State Fund building.
- May 2011 – At the request of Mary sexton, DNRC Trust Land staff begin discussions with DOA staff concerning possible acquisition of the old Corrections property.
- March 2012 – Appraisal of the property completed by Mike Joki, Highest and Best Use analysis indicates redevelopment with a new office building, sets the value as a vacant site at \$803,000, estimated demolition costs are \$350,000.
- September 2012 – as part of due diligence to acquire the property DNRC acquires estimates for both renovation and redevelopment of the site from Diamond Construction, Helena, MT.
- December 2012 – Land Board approves administrative transfer of property from DOA to DNRC at the appraised value less demolition costs estimated in appraisal. Total costs to UM and MSU trusts, \$435,000.
- February 2013 – DNRC closes transaction and works with DOA to “mothball” the building.
- March 2013 to May 2014 – DNRC works with DOA to draft a Request for Proposal for 1.) a ground lease of the site and 2.) a developer to provide office space on the site that DNRC would lease.
- December 2013 - Appraisal of the property updated by Mike Joki, Highest and Best Use analysis still indicates redevelopment with a new office building, sets the value as a vacant site at \$778,000, estimated demolition costs are \$370,000.
- May 9, 2014 – Request for Proposal issued, primary objective is to secure a ground lessee, and lease-back of office space for DNRC.
- May 21, 2014 – Pre-proposal conference and walk through with potential developers, Dick Anderson, Diamond Construction, and Golden Eagle Construction.
- August 2014 – RFP response due date, one proposal submitted by Dick Anderson. Proposal is for demolition and redevelopment of site with a new three story office building with a two story parking structure.

- September 16, 2014 – Proposal scoring meeting by DOA and DNRC, determine if proposal meets requirements of RFP.
- August- September 2014 – MEPA analysis.
- November 2014- Land Board approval for commercial ground lease and redevelopment of the site.
- December 2014- Commercial ground lease and build to suit leases are executed.
- January 2015- Demolition of Mills Hall commences.

Schiltz, Tricia

From: Bacon, Garrett
Sent: Friday, February 06, 2015 10:18 AM
To: Beck, Ray; Schiltz, Tricia; Thomas, Shawn; Tubbs, John
Cc: Bacon, Garrett
Subject: FW: DNRC -----lease comps

Below are some older buildings in Helena that we currently lease that are not comparable to a new "built to suit" building like the DNRC project but they are currently paying similar rental rates.

<u>Lease #</u>	<u>square feet leased</u>	<u>Rate</u>
#6163	9,191 sq ft	\$24.00 (20 year+ old building. "as is" space)
#4646	20,708 sq ft	\$22.94 (30+ year old building. Space was remodeled to fit our needs)
#1201	7,200 sq ft	\$24.61 (10 year old Building was a "build to suit" building near Campus and the leasing state agency. They needed this building to be in proximity with their other 2 locations)
#8114	9,640	\$22.50 (30 year old building. Some remodeling to fit our need.)
#8094	8,940	\$21.00 (30 year old building. Little remodeling -basically "as is")

We did not factor in/include rental rates from the Great Northern or other high end leased space rates as they are in the \$30 per square foot range.

To get a new building, like DNRC is proposing, that is designed from the ground up around their exact space need for a rate of \$24.75 per sq ft for 20 years without any CPI-U or other annual inflation factor makes this space a very good leased premise. When you consider the fact that this project is on state leased land, in very close proximity to the Capitol Complex and other DNRC space, this project is very reasonable.

Shawn, I pulled this together rather quickly because of your timeline. I am in the middle of numerous other legislative requests but if something more comes to mind, I will pass it forward.

Garrett M. Bacon
Leasing Officer
State of Montana, Department of Administration
General Services Division
1310 East Lockey
Helena, Montana, 59620-110
406-444-3108
E mail: gbacon@mt.gov